China / Hong Kong Company Update

Link REIT

Bloomberg: 823 HK EQUITY | Reuters: 0823.HK

Refer to important disclosures at the end of this report

DBS Group Research . Equity

4 Apr 2022

BUY

Last Traded Price (1 Apr 2022): HK$67.65 (HSI : 22,040)
Price Target 12-mth: HK$82.00 (21% upside) (Prev HK$83.30)

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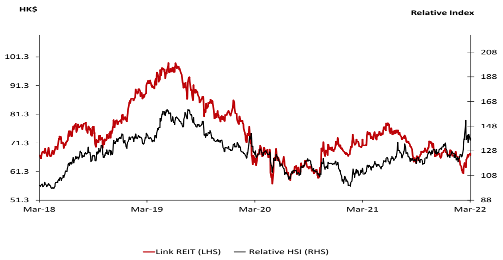
What's New

- Hong Kong retail reversionary growth should remain positive in FY22 despite the disruption from Omicron
- A new HK$120m tenant support scheme is in place, revised down distribution income for FY22-23 by 2-3%
- Renovation works at Happy Valley Shopping Mall to commence soon
- Maintain BUY with DDM-based TP of HK$82

Price Relative



Forecasts and Valuation

FY Mar (HK$ m)	2020A	2021A	2022F	2023F
Gross Revenue	10,718	10,744	11,625	12,509
Net Property Inc	8,220	8,238	8,859	9,587
Net Profit	(17,122)	1,185	6,285	6,631
Distribution Inc	5,965	6,010	6,655	6,711
DPU (HK$)	2.87	2.90	3.20	3.22
DPU Gth (%)	6	1	10	1
Div Yield (%)	4.2	4.3	4.7	4.8
Gross Gearing (%)	17	18	24	25
Book Value (HK$)	77.61	76.64	79.05	82.18
P/Book Value (x)	0.9	0.9	0.9	0.8
DPU Rev (%):			(2)	(3)
Consensus DPU (HK$):			3.08	3.25
Other Broker Recs:		B:19	S:0	H:0

Source of all data on this page: Company, DBS Bank (Hong Kong) Limited ("DBS HK"), Thomson Reuters

Resilience in turbulent times

Investment Thesis

BUY with HK$82 TP. Link REIT offers distribution yields of 4.7-4.8% for FY22-23. Despite the disruption led by the COVID resurgence in Hong Kong and China, Link REIT's earnings should remain resilient with ongoing acquisitions to augment growth.

Embracing the COVID challenges. While the fifth wave of the pandemic led to a setback of tenant sales recovery in 4QFY22, reversionary growth should remain in the positive territory in FY22. Link REIT has been running a new HK$120m tenant support scheme since early Feb. With gradual easing of social distancing measures and distribution of consumption vouchers from Apr-22, domestic consumption should recover, thus benefitting Link REIT.

More acquisitions expected to come. Since Oct/Nov 21, Link REIT has announced a string of asset acquisitions in Hong Kong, China, and Australia, worth >HK$13bn. With gearing comfortable at c.25%, Link REIT is expected to pursue more accretive acquisitions, especially in China and overseas, given its Vision 2025. This should augment and diversify its asset and earnings base. The planned disposal of Stanley Plaza, if materializes, could free up capital to fund acquisitions. This will enable Link REIT to grow its portfolio, without overstretching its balance sheet.

Valuation:

Link REIT provides unit holders with a relatively visible and steady distribution income stream. Thus, the Dividend Discount Model (DDM) would be the most appropriate valuation method. Under the DDM approach, the target price of Link REIT is equal to the discounted value of all future distributions paid with assumed discount rates of 6.6% and terminal growth of 2%.

Where we differ:

We believe that the gradual relaxation of social distancing measures and distribution of consumption vouchers from Apr should result in the release of pent-up demand for consumption. The REIT's community malls should be less vulnerable to the accelerating online shopping trend.

Key Risks to Our View:

Further delays in recovery of domestic consumption due to the prolonged pandemic would impact retail rental income. Any faster-than-expected interest rate hike would adversely affect its distribution and valuation.

At A Glance

Issued Capital (m shrs)	2,082
Mkt Cap (HK$m/US$m)	140,847 / 17,980
Major Shareholders (%)	
APG Asset Management N.V.	5.4
State Street Global Advisors Asia Ltd.	5.3
Free Float (%)	100
3m Avg. Daily Val. (US$m)	48.30
GICS Industry: Real Estate / Equity Real Estate Investment	

WHAT'S NEW

Positive reversionary growth sustainable in FY3/22

Aided by improved pandemic situation and distribution of electronic consumption vouchers, overall tenant sales growth at Link REIT's Hong Kong retail portfolio accelerated to 10.4% in 3QFY22 from 1HFY22's 8.9%. This was primarily driven by stronger tenant sales from general retail trades which grew by a larger 14.6% in 3QFY22, compared to 13.4% in 1HFY22. Tenant sales decline for supermarket and foodstuff trades also narrowed to 6% in 3QFY22 from 1HFY22's 8.6%. Receipts from F&B tenants continued to register robust growth of 25.4% in 3QFY22 (1HFY22: 25.7%). This brought the overall occupancy cost ratio further down to 12.8% in 3QFY22 from 1HFY22's 13%, lowest since the outbreak of COVID-19.

However, the fast spread of the Omicron variant and tightening of social distancing measures since early 2022 has taken a toll on the retail market recovery. Tenant sales growth in 4QFY22 (or 1Q22) should return to negative territory with F&B sector taking the hardest hit from dine-in restrictions. Sales of general retail trades should be dampened by sluggish consumer sentiment. On the other hand, supermarket sales should resume positive growth as tightened social distancing measures is driving demand for groceries.

Rental reversion of Hong Kong retail portfolio has turned positive at 3.4% in 1HFY22 on the back of domestic consumption recovery. Despite recent disruptions led by the COVID resurgence, we expect Link REIT's retail rental reversion to remain positive for FY22. If the fifth wave of the pandemic can be brought under control in the near term, reversionary growth could stay slightly positive in FY23 in our view.

Hong Kong retail portfolio occupancy reached a record high of 97.9% as of Dec-21 (Sep-21: 97.5%). Compared to 2020, existing retail tenants have become more experienced in coping with challenges led by the COVID resurgence. Selected tenants that are severely impacted are seeking for lease restructuring and rental concession. Hence, the impact from the proposed new law on rental enforcement moratorium should not be overplayed.

Link REIT has been running a new round of tenant support scheme, amounting to HK$120m, since early Feb. Rental concessions are offered to retail tenants on a case-by-case basis with a priority to those severely impacted by social distancing protocols including fitness centers, beauty salons and Chinese restaurants. In 2020, Link REIT had established a tenant support scheme amounting to HK$600m, with c.HK$500m being utilised ultimately.

Including Happy Valley shopping mall, Link REIT's China retail portfolio was 92.4% let as of Dec-21 (Sep-21: 91.5%). Link REIT has completed the asset enhancement work at Link CentralWalk in Shenzhen, with grand re-opening in Jan-22. With the number of shops increasing by 20% post renovation, Link CentralWalk provides more diversified retail offering, catering to the shopping need of young shoppers, office workers in the surrounding areas and family-oriented customers.

Link REIT plans to renovate the newly acquired Happy Valley shopping mall in Guangzhou, marking its second AEI in China. Link REIT has completed the planning and design for ex-department store space which will become the new annex of the mall. The renovation works are expected to commence in 3Q22 and last throughout FY23.

Despite intense competition in Shanghai office market, occupancy at Link Square remained firm at 95.1% in Dec-21 (Sep-21:96.7%). Link REIT is upgrading major facilities including reception lobby and public areas with target completion in mid-22 to enhance the property's competitiveness.

Following the proactive acquisition since late 2021, Link REIT's pro-forma gearing ratio stands at 24.6%. China and overseas assets accounted for 16.5% and 7.6% of Link REIT's total portfolio valuation, falling short of its management's guidance of 20-25% and 10-15% respectively. In addition to organic growth, more acquisitions are expected to help the REIT achieve its Vision 2025 strategy, which aims for high single digit CAGR growth in AUM.

In Feb-22, in view of the unsolicited expression of interest towards Stanley Plaza, Link REIT invited interest from the market to purchase the property on a standalone basis. The disposal of Stanley Plaza, if materialized, could free up capital for future acquisitions. If this private tender receives strong market interest, we do not rule out the possibility of Link REIT disposing more mature assets in Hong Kong. This should enable Link REIT to expand and diversify its property portfolio without overstretching its balance sheet.

On the other hand, Link REIT has submitted a tender for the design, construction, and operation of Artist Square Towers project at West Kowloon Cultural District. Comprising three commercial towers, the project sets to offer a total GFA of 0.7msf including 0.67msf for office space and the balance for retail use.

We have revised down our FY22 and FY23 DPU forecast by 2-3% respectively to reflect mainly the impact of rental relief and lockdowns in China.

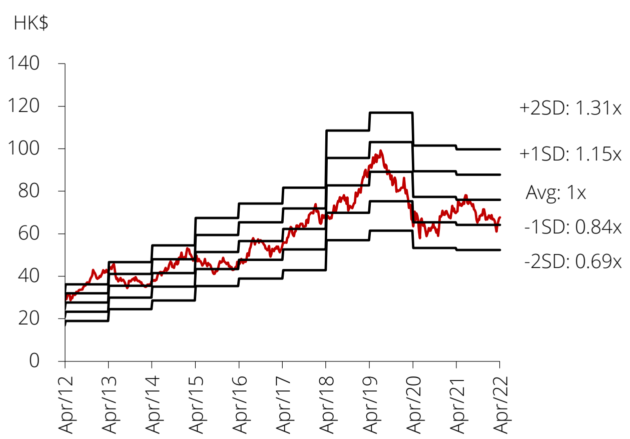
Link REIT is trading at 4.7-4.8% distribution yields for FY22-23. This translates into yield spread of 2.5%, same as its 10-year average. The government plans to ease social distancing measures starting from Apr-22. This should release pent-up demand for consumption with distribution of consumption vouchers giving an additional boost. Continued asset acquisitions should enhance and diversify its earnings. Any positive news flow on asset disposal should prompt stock price appreciation. Hence, we maintain BUY with a DDM-based TP of HK$82. Any faster-than-expected interest rate hike should be among the key investment risks for Link REIT which is a bond-like investment.

Company Background

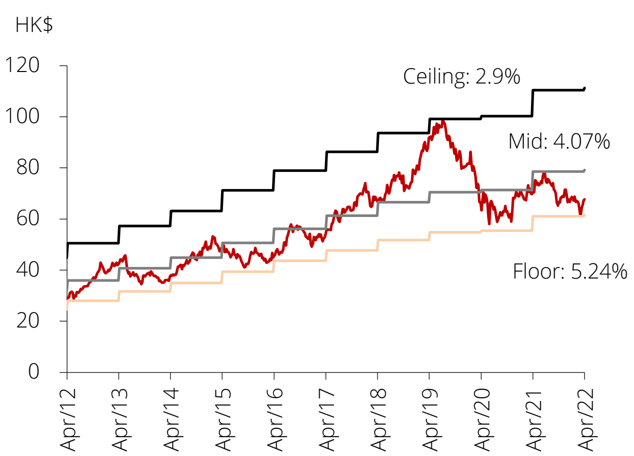
Link REIT is the largest listed REIT in Hong Kong. Its portfolio comprises mainly retail properties located adjacent to public housing estates and has a 60% stake in The Quayside in Kwun Tong. In China, Link REIT holds a portfolio of neighborhood malls in first-tier cities mainly Beijing, Guangzhou, Shanghai and Shenzhen and an office property in Shanghai. In 2020, Link REIT expanded its presence in overseas office market by acquiring 100 Market Street in Sydney and The Cabot in London. In Oct-21, Link REIT made its maiden foray into the China logistics property market by acquiring 75% stake of two modern warehouses in Dongguan and Foshan. In Nov-21, Link REIT acquired 50% interests in three retail properties in Sydney, marking its first venture in the Australian retail market. In the same month, Link REIT purchased a godown in Chai Wan and a mixed-use car parking building in Hung Hom. In Feb-22, Link REIT further expanded its office presence in Australia.

Price to book NAV band and historical yield band

Price to book NAV band



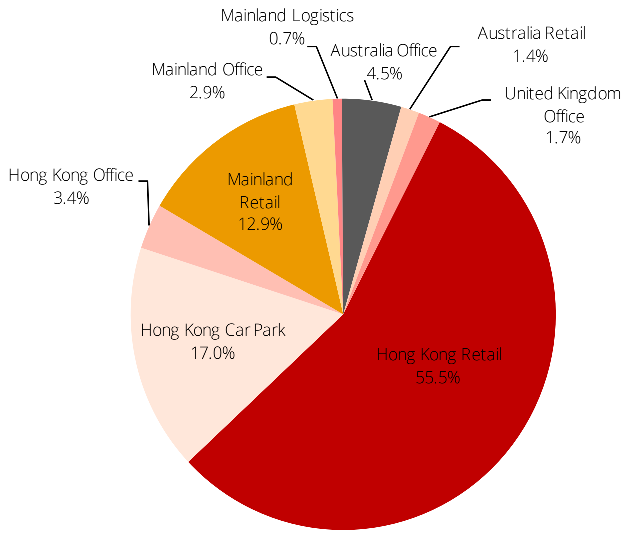
Historical yield band



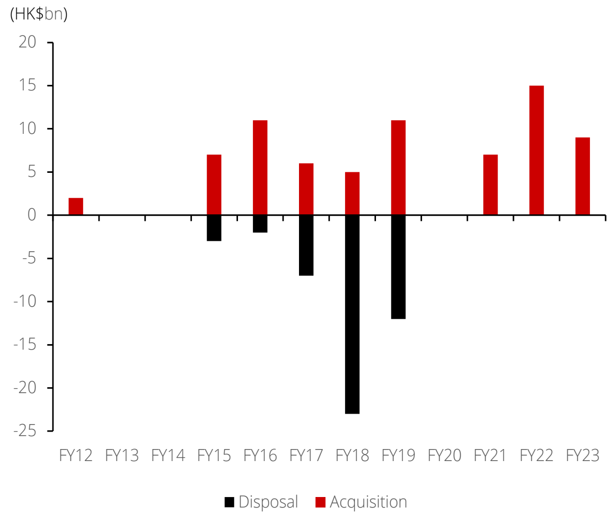
Source: Bloomberg Finance L.P. DBS HK

Property Portfolio

Breakdown of property portfolio



Portfolio recycling



Source: Link REIT

Recent property acquisitions

Date	Properties	Location	Stake (%)
Apr-21	Qibao Vanke Plaza	Shanghai	50
Jun-21	Happy Valley Shopping Mall	Guangzhou	100
Oct-21	Two modern warehouses	Dongguan & Foshan	75
Dec-21	Two Institutional Grade Car Park/ Car Service Centres and Godown Buildings	Chai Wan & Hung Hom	100
1H22	Three retail properties	Sydney	50
1H22	JV in a prime office portfolio	Sydney & Melbourne	49.4

Source: Link REIT

Key Assumptions (%)

	2022F	2023F
Retail rental (Shopping centre) -HK	0	5

Source: Company, DBS HK

Segmental Breakdown (HK$ m)

FY Mar	2019A	2020A	2021A	2022F	2023F
Revenues (HK$ m)					
Retail and commercial	7,648	7,626	7,787	8,281	9,038
Car parks	1,979	1,912	1,883	2,059	2,134
Other revenues	410	1,180	1,074	1,286	1,337
Total	10,037	10,718	10,744	11,625	12,509

Source: Company, DBS HK

Income Statement (HK$ m)

FY Mar	2019A	2020A	2021A	2022F	2023F
Gross revenue	10,037	10,718	10,744	11,625	12,509
Property expenses	(2,348)	(2,498)	(2,506)	(2,766)	(2,922)
Net Property Income	7,689	8,220	8,238	8,859	9,587
Other expenses	(405)	(416)	(428)	(454)	(479)
Joint ventures	0	0	0	125	404
Interest (Exp)/Inc	(513)	(447)	(644)	(1,002)	(1,492)
Exceptionals	15,030	(23,948)	(5,322)	0	0
Pre-Tax Profit	21,801	(16,591)	1,844	7,528	8,020
Tax	(1,359)	(712)	(1,092)	(1,205)	(1,307)
Non-Controlling Interests	(113)	181	433	(39)	(82)
Net Profit	20,329	(17,122)	1,185	6,285	6,631
Distribution income	5,723	5,965	6,010	6,655	6,711
Revenue Gth (%)	0	7	0	8	8
NPI Gth (%)	0	7	0	8	8
Dist. Inc Growth (%)	5	4	1	11	1
DPU Growth (%)	9	6	1	10	1

Source: Company, DBS HK

Balance Sheet (HK$ m)

FY Mar	2019A	2020A	2021A	2022F	2023F
Fixed Assets	218,634	194,613	200,375	218,200	225,259
Other LT Assets	36	231	218	218	218
Intangibles Assets	433	424	392	392	392
Associates/JVs	0	0	0	10,108	10,513
Bank Balance/Cash & Liquid	6,789	7,877	2,530	1,945	4,593
ST Investments	0	2,746	2,742	2,742	2,742
Inventory	0	0	0	0	0
Debtors	933	1,231	1,195	1,205	1,215
Other Non Cash Current	112	497	2,433	128	128
Total Assets	226,937	207,619	209,885	234,939	245,060
ST Debt	3,367	937	3,248	5,682	15,482
Creditors	2,585	2,640	2,504	2,494	2,484
Other Current Liab	2,174	2,278	2,893	2,923	2,953
LT Debt	20,850	33,661	35,388	51,682	45,382
Deferred Tax Liabilities	3,191	2,871	3,029	3,029	3,029
Other LT Liabilities	5,444	5,115	4,130	4,130	4,130
Non-Controlling Interests	587	406	(27)	421	503
Unitholders' funds	188,739	159,711	158,720	164,578	171,097
Total Capital	226,937	207,619	209,885	234,939	245,060
Share Capital (m)	2,109	2,057	2,071	2,082	2,082
Gross Debt	(24,217)	(34,598)	(38,636)	(57,364)	(60,864)
Working Capital	(292)	6,496	255	(5,079)	(12,241)
Book NAV (HK$)	89.48	77.64	76.64	79.05	82.18
Gross Gearing (%)	11	17	18	24	25

Source: DBS HK

Cash Flow Statement (HK$ m)

FY Mar	2019A	2020A	2021A	2022F	2023F
Pre-Tax Income	21,801	(16,591)	1,844	7,528	8,020
Associates' Profits	0	0	0	(125)	(404)
Tax Paid	(1,102)	(933)	(737)	(1,205)	(1,307)
Depr/Amort	22	75	75	75	75
Disposal of FAs/Subsidaries	(2,761)	15	0	0	0
Chg in Wkg.Cap.	(204)	(282)	(70)	10	10
Other Non-Cash	(11,766)	24,305	5,966	1,002	1,492
Operational CF	5,990	6,589	7,078	7,286	7,886
Net Capex	2,253	(1,673)	(8,375)	(11,928)	(625)
Net change in asso/jv	0	0	0	(9,984)	0
Net Change in Investments	0	(2,777)	0	0	0
Assoc, MI, Invsmt	4,522	3,918	(2,167)	2,395	90
Investment CF	6,775	(532)	(10,542)	(19,517)	(535)
Net Chg in Debt	(4,320)	10,129	3,169	18,728	3,500
New issues/Unit Buyback	(3,216)	(4,240)	(379)	0	0
Distribution Paid	(5,517)	(5,930)	(3,966)	(6,399)	(6,621)
Other Financing CF	(89)	(725)	(884)	(683)	(1,582)
Financing CF	(13,142)	(766)	(2,060)	11,646	(4,703)
Chg in Cash	(377)	5,291	(5,524)	(585)	2,648

Source: Company, DBS HK

Target Price & Ratings History

S.No.	Date	Closing Price	12-mth Target Price	Rating
1:	14-Apr-21	HK$71.90	HK$79.35	Buy
2:	7-Jun-21	HK$74.10	HK$80.40	Buy
3:	18-Jun-21	HK$75.55	HK$80.65	Buy
4:	8-Oct-21	HK$65.90	HK$80.65	Buy
5:	8-Nov-21	HK$68.70	HK$81.45	Buy
6:	11-Nov-21	HK$70.40	HK$82.80	Buy
7:	11-Feb-22	HK$68.00	HK$83.30	Buy

Source: DBS HK

Analyst: Jeff Yau
Percy Leung

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BUY (>15% total return over the next 12 months for small caps, >10% for large caps)
HOLD (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)
FULLY VALUED (negative total return, i.e., > -10% over the next 12 months)
SELL (negative total return of > -20% over the next 3 months, with identifiable share price catalysts within this time frame)

**Share price appreciation + dividends*

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